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In the Supreme Court of the United States

OCTOBER TERM, 1944

No. 1233

THE NATIONAL BRONX BANK OF NEW YORK,
PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The findings of fact and memorandum opinion of the Tax Court (R. 19–30) are unreported; the opinion of the Circuit Court of Appeals (R. 203–205) is reported at 147 F. 2d 651.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on February 27, 1945 (R. 206). The petition for a writ of certiorari was filed on May 3, 1945. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the Tax Court erred in holding that bond write-downs, made at the order of a national bank examiner and taken by the petitioner as bad debt deductions without challenge by the Commissioner, should not be restored to the cost basis of the bonds for the purpose of computing gain or loss on their sale in the taxable years irrespective of whether the deductions in the prior years were of any tax advantage to petitioner.

STATUTES AND REGULATIONS INVOLVED

The pertinent statutes and regulations are set forth in the Appendix, *infra*, pp. 7–9.

STATEMENT

The facts as found by the Tax Court (R. 20–25) may be summarized as follows:

The petitioner, a national banking association, was incorporated in 1926 (R. 20). Its income tax returns for the taxable years involved were made on the accrual basis and were filed with the Collector of Internal Revenue for the Fourteenth District of New York (R. 20).

In the years 1932, 1933, 1935 and 1936, a national bank examiner ordered the petitioner to write down on its books the value of certain bonds held by it (R. 20). The securities, the date acquired by the petitioner, the par value of the bonds, the amount and years of write-downs, the write-down value in the years the bonds were eventually sold, the selling price, and the loss or gain based upon the write-down

value and based upon cost, are all set forth in the opinion of the Tax Court (R. 21). The petitioner claimed the amounts of the write-downs as deductions for bad debts on its returns for the years 1932, 1933, 1935 and 1936, and the returns were accepted by the Commissioner as filed (R. 22). The bonds written down were worthless to the extent of the write-downs, and were then ascertained to be worthless by the petitioner (R. 25). The petitioner realized a tax benefit of $3,334.93 in 1936 from the write-down deductions; no tax benefits resulted from the deductions in the other years (R. 22–23). In 1938 and 1939, the petitioner sold the bonds involved, and in its returns for those years claimed loss deductions, using the original cost of the bonds to it as a basis (R. 25). The Commissioner disallowed the deductions on the ground that the basis to be used was the cost less the amounts written down and deducted in the petitioner's returns for prior years.

The Tax Court held that the cost basis of the bonds sold in 1938 and 1939 should be reduced in the amount of the write-down deductions previously claimed and allowed, and sustained the Commissioner's determination that a deficiency existed (R. 30). The Circuit Court of Appeals affirmed (R. 206).

ARGUMENT

The Tax Court found as facts (R. 29–30) that the bonds written down in the years 1932, 1933, 1935 and 1936, were then worthless to the extent of the amount of the write-downs, were then ascertained to be so worthless, and were then duly charged off by

the petitioner bank. That there was substantial evidence in the record to support these findings seems clear. The write-downs were in fact made; they were claimed as deductions by the petitioner in its tax returns for the years of their making; and the bonds were sold at a figure substantially in accord with the losses claimed.[1] No evidence was adduced to fix the time of the losses in some period other than the ones in which the write-downs were made. Section 113 (b) (1) (A) of the applicable acts (Appendix, *infra*, p. 8) consequently required the adjustment made by the Commissioner in respect of the basis of the bonds.

It is true that the impetus for the write-downs came in the first instance from the bank examiner's order, but, needless to say, the examiner had nothing to do with petitioner's taking the bad debt deductions in its tax returns. It did this entirely of its own volition. As the bad debt provisions of the applicable acts make clear (Appendix, *infra*, p. 7), petitioner had the option of claiming or not claiming partial worthlessness quite as it saw fit.

[1] All of the bonds involved, except for one group of International Tel. and Tel. bonds, were written down to a value lower than par (R. 21). The fact that these International Tel. and Tel. bonds were only written down to par does not deprive the Tax Court's finding that they were partially worthless of evidentiary support, because, even assuming that par value and not cost is the basis upon which partial worthlessness should be calculated, for all that appears in the record International Tel. and Tel. may not have been petitioner's primary debtor. These bonds may have been acquired from a third person as collateral on a debt larger than the par value of the bonds.

There was no question of its making a claim in the years of the write-downs or forever holding its peace. *Eljer Co.* v. *Commissioner*, 134 F. 2d 251 (C. C. A. 3d), and cases cited therein. See also *Bingham* v. *Commissioner*, 105 F. 2d 971 (C. C. A. 2d). Hence it seems to us manifest that there is no merit to petitioner's plea that its action in writing down the bonds in the earlier years cannot be regarded as an ascertainment of worthlessness because involuntary. Plainly it "ratified" the examiner's appraisal when it took the deductions. There was further "ratification" of the *fact* of then partial worthlessness when the bonds were sold at approximately the write-down figures.

There is no more merit, in our view, to petitioner's contention that some of the former deductions, claimed by the petitioner and accepted by the Commissioner (R. 22), must themselves now be disregarded because they resulted in no tax benefit when taken. Neither the language in *Dobson* v. *Commissioner*, 320 U. S. 489, 505, rehearing denied, 321 U. S. 231, with respect to what might be termed the tax benefit theory, nor Section 116 (a) (12) of the Revenue Act of 1942 has any application here. For this Court, in the *Dobson* case, was speaking of the tax treatment of recoveries of amounts previously written off and deducted in years when deductions brought no tax advantage; that is also the subject of the statute to which we have just made reference. But the subject matter of the controversy at bar is

not recoveries and is not related to recoveries; we are here concerned not with whether an item should be taxed as income, but with whether the cost basis of an item shall be reduced by the amount of a once-allowed deduction. The Tax Court properly held that a taxpayer may not restore to its cost basis the amounts previously—and properly—allowed as deductions. Cf. *Virginian Hotel Corp.* v. *Helvering*, 319 U. S. 523.

CONCLUSION

There is no warrant for further review. The Tax Court's decision was entitled to affirmance, for its findings of fact were based on substantial evidence and, beyond that, the only other issue is one of proper tax accounting. *Dobson* v. *Commissioner*, *supra*. For these reasons, and because there is no conflict, the petition should be denied.

Respectfully submitted.

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MAY 1945.